

No. 21967 ✓

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

C. DOUGLAS WIKLE, Trustee in Bankruptcy, for
Nevada Henderson Land Co., a corporation,

Appellant,

vs.

COUNTRY LIFE INSURANCE COMPANY, *et al.*,

Appellees.

On Appeal From the United States District Court for the
Central District of California.

APPELLANT'S OPENING BRIEF.

JOSEPH S. POTTS,

840 North Birch Street,
Santa Ana, Calif. 92701,

Attorney for Appellant.

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APPELLANT'S OPENING BRIEF.

I.

Jurisdictional Statement.

This is an appeal from an Order entered on March 8, 1967, by the United States District Court, Central District of California (page 484 of the Transcript of Record on Appeal), hereinafter designated as "R", which Order affirmed the Referee's Order of October 28, 1966 [R. p. 409], dismissing the Trustee's Application to Quiet Title, "without prejudice".

The Trustee's present appeal from the aforesaid District Court Order has been duly perfected under the provisions of Sec. 24, Subsections (a) and (b), of the National Bankruptcy Act (11 U.S.C., Sec. 47(a)(b)), which constitutes the jurisdictional basis therefor.

Statement of the Case.

The Referee's aforesaid Order of October 28, 1966, was the result of proceedings commenced by appellant's "Application for Order to Show Cause to: (1) Quiet Title to Real Property; (2) For Declaratory Relief with Respect Thereto; and (3) Cancellation of Documents Constituting a Cloud on Title of Such Real Property", dated June 29, 1966 [R. p. 235], and the "Order to Show Cause Re Real Property" issued thereon, dated June 30, 1966 [R. p. 252].

None of the respondents, now appellees on appeal, filed an answer to appellant's above-described application of June 29, 1966; instead, they merely filed written objections to the jurisdiction of the bankruptcy court. At this point, it should be noted that one of the remarkable features of this unique case (and the latter term is used advisedly, and despite an awareness of the general propensity of attorneys to view their own case as "unique" or "remarkable") is the fact that not one scintilla of oral testimony, nor one scrap of documentary evidence has been formally introduced despite the following facts: (1) the case has been pending for almost two years; (2) the file, conservatively, is several inches thick with pleadings, documents, appraisal reports, briefs, etc., and (3) there is involved, conservatively, an equity in real property in excess of One Million Dollars (\$1,000,000.00).

Furthermore, the failure of the courts below to admit evidence in a case of such obvious importance is all the

more puzzling in light of the overwhelming authority for the proposition that in all instances in which its jurisdiction is challenged the bankruptcy court has:

“ . . . in every case, jurisdiction to determine whether it has possession, actual or constructive. It may conclude, where it lacks actual possession, that the physical possession held by some other persons is of such a nature that the property is constructively within the possession of the court.” (*Taubel-Scott-Kitzmiller Co., Inc. v. Fox*, 264 U.S. 426, 44 S. Ct. 396, 68 L. Ed. 770. See, also, *Wuchner v. Goggin* (9th Cir., 1949), 175 F. 2d 261).

See, further, 2 Collier on Bankruptcy, Para. 23.07, page 519, *et seq.*, in which the following appears at pages 521, 522:

“A necessary corollary to these principles is that in all proceedings to recover summarily the possession of property from the hands of third persons, ‘there is preliminary jurisdiction to inquire into the nature of the defendants’ possession and any adverse claim so far as to see whether it is more than colorable’ (quoting from *Chandler v. Perry*, (5th Cir.) 74 F. 2d 371, which, in turn, cited *Mueller v. Nugent*, 184 U.S. 1, 22 S. Ct. 269, 46 L. Ed. 405). In other words, it becomes necessary for the court to determine as to the substantiality of the adverse claim, if any, prior to assuming summary possession of the property *and for this reason the court may make its inquiry into the basis of the claim. The mere assertion of an adverse claim is not enough to prevent the exer-*

cise of summary jurisdiction by the bankruptcy court; but in all cases the claimant is entitled to be heard." (Emphasis added).

In the anomalous posture of the case, arising from the fact that no formal evidence has ever been introduced, it is submitted that the allegations of appellant's Application must be taken as admitted under Local Rule 222 and Rule 8(d) Federal Rules of Civil Procedure. Thus, in *Moore v. Linahan* (2nd Cir., 1941), 117 F. 2d 140, *cert. den.*, 314 U.S. 628, 62 S. Ct. 59, 86 L. Ed. 504, the court held that facts alleged in an involuntary petition for corporate reorganization were admitted by failure to deny them. Similarly, in *Zydney v. New York Credit Mens' Ass'n.* (2nd Cir., 1940), 113 F. 2d 986, it was held that where an "answering affidavit" of a trustee in bankruptcy to a petition in reclamation was merely argument based upon testimony of the petitioner and officers of the bankrupt when examined by the trustee, such affidavit was *not* an "answer", and the petition, accordingly, stood as admitted (See, also, *Sun Maid Raisin Growers' Ass'n. v. Neustadter Bros.* (9th Cir., 1941), 115 F. 2d 126).

Another very material result of (1) appellees' failure to file answers, and (2) the fact that no formal evidence, as such, has been introduced, is the effect of this upon the scope of review. Thus, the law is clear that where, as here, the facts are not in dispute, a Referee's deductions or inferences, as well as his conclusions of law, therefrom, are *not* within the so-called "clearly erroneous" doctrine, and, accordingly, are *not* binding on the reviewing or appellate court (*Tepper v. Chichester* (9th Cir., 1960), 285 F. 2d 309, 312; *In re De Jay Stores, Inc.* (D.C., N.Y. 1963), 220 F. Supp. 497,

500; *In re Stewart* (D.C., Ore., 1964), 233 F. Supp. 89, 91; *In re Itemlab, Inc.* (D.C., N.Y., 1966), 257 F. Supp. 764). The theory, of course, is that in such circumstances, the reviewing or appellate court is at least as competent as the Referee to draw inferences and conclusions of law from admitted or undisputed facts.

Accordingly, appellant's aforementioned application, dated June 29, 1966, is incorporated herein by reference as though set forth herein in full. However, the following "summary" of the facts as alleged therein, as well as certain additional facts admitted by some of appellees' pleadings and briefs, is set forth for the court's convenience, as follows: the instant case was commenced on January 4, 1966, by the filing of a Petition for an Arrangement under the provisions of Chapter XI of the Bankruptcy Act. This petition was filed on the debtor's behalf by its attorney, Mr. Burke Mathes. (We will consider at some length hereinbelow, appellee's belated, and, we submit totally unfounded, assertions that the proceeding somehow became a "straight bankruptcy" proceeding on January 13, 1966).

On January 4, 1966, the then debtor corporation was the undisputed owner of record of a convalescent hospital commonly known as 2940 W. Whipple Avenue, Redwood City, California (in San Mateo County), which hospital was designated as "Sunshine Convalescent Hospital". Also, on said date, the property was subject to the following encumbrances of record: (1) a first trust deed held by Country Life Insurance Company, an Illinois corporation, hereinafter referred to as "Country Life", securing an indebtedness in the original principal sum of \$900,000.00; (2) a second trust deed now in favor of Ropat Investment Company, hereinafter

referred to as "Ropat", Universal Surgical Supply, Inc., hereinafter referred to as "Universal", and Casavic, S.A., a Mexican corporation, hereinafter referred to as "Casavic", and (3) a third trust deed in favor of J. G. Richardson and George B. McClyman, hereinafter referred to as "Richardson" and "McClyman", respectively. Although the original principal indebtednesses secured by the second and third trust deeds were \$200,000.00, and \$172,000.00, respectively, the beneficiaries under said trust deeds have agreed in writing, as alleged in Paragraph XIII of the appellant's Application, to execute reconveyances in consideration of payment of an aggregate of \$100,000.00, for *all* interests in both said second and third trust deeds.

As alleged in Paragraph XII of appellant's Application, the fair market value of the convalescent hospital is "not less than \$2,185,000.00". In this connection, Referee Bergener, on his own motion, appointed one Joseph Donovan to appraise the property. Mr. Donovan's appraisal on file herein, dated May 26, 1966, is in the sum of \$1,900,000.00.

Since the property was purportedly sold under the power of sale, after bankruptcy, and under highly questionable circumstances, to Country Life, for \$871,191.97, a sum slightly less than the balance then owing Country Life, it is obvious that *a most substantial equity* has "gone down the drain" unless, as we strongly urge, this court has the power, jurisdiction and duty to set aside the wholly improper and invalid orders pursuant to which Country Life purported to cause the property to be sold.

On January 6, 1966, Referee Bergener appointed appellant, presently trustee, as the Chapter XI receiver.

Appellant was later appointed trustee on or about March 29, 1966, shortly after the entry of an order adjudicating the debtor corporation a bankrupt.

Prior to the debtor's filing of its Petition for an Arrangement on January 4, 1966, Country Life had commenced the procedural steps preliminary to a sale of the property in issue under the power of sale contained in its trust deed, and *subsequently* Country Life filed an action in the Superior Court of San Mateo County, solely for "Specific Performance" of rental collection provisions contained in its trust deed, in which it prayed for the appointment of a state court receiver to collect the rents owing on the debtor's convalescent hospital. However, as admitted in one of Country Life's own pleadings filed herein, to wit: its memorandum in support of its motion to dismiss the debtor's Chapter X petition, filed on January 17, 1966 [R. p. 74], *in truth and in fact, the hospital was closed and not in operation, hence there were no rents to be collected*. Thus, commencing at page 1, line 30, to page 2, line 3, of Country Life's last-mentioned document, the following is stated:

"The debtor's sole asset is real estate in San Mateo, California (sic) upon which a hospital has been constructed. *The hospital has since been closed and not in operation since November, 1965*". (Emphasis added).

On November 15, 1965, the Superior Court entered an order appointing a receiver to collect non-existing rents from non-existing tenants! As alleged in appellant's Application, the state court receiver never took possession of the debtor's real property and, quite obviously, never collected any rents.

As will be pointed out hereinbelow, it was the pendency of this specific performance action, which Country Life misrepresented to Referee Bergener to be a "foreclosure proceeding", and the wholly spurious "receivership", which counsel for Country Life urged as depriving the bankruptcy court of jurisdiction, and all this despite the fact that Country Life, in fact, at all times intended to cause the property to be sold extrajudicially, which fact it conveniently neglected to inform Referee Bergener at the hearing of January 13, 1966.

Concomitantly with the filing of the Chapter XI petition on January 4, 1966, Mr. Mathes, as counsel for the then debtor, procured an order restraining Country Life from causing the debtor's real property to be sold on January 5, 1966, under the power of sale, pending a hearing set before Referee Bergener on January 13, 1966. Likewise on the date he filed the Chapter XI proceeding, Mr. Mathes procured a further, and very common, order granting the debtor ten (10) days within which to file its schedules, etc. On the same date as the hearing on the aforementioned restraining order, viz.: January 13, 1966, the debtor's schedules were filed; however, by obvious inadvertence or oversight, counsel for the debtor overlooked substituting for the printed form "Petition", applicable to normal bankruptcy proceedings, a special page referring instead to Chapter XI. That this was unintentional and purely inadvertent is clearly evident from the fact that counsel for the debtor filed subsequent documents making reference to the pendency of a Chapter XI proceeding (*e.g.*, the Order of Reference under Chapter X filed January 19, 1966 [R. p. 87], *inter alia*, bears the double caption: "In Proceedings for an Arrangement" and "In Pro-

ceedings for the Reorganization of a Corporation”), However, since Referee Bergener did not see fit to permit evidence to be introduced, appellant appended an affidavit of Mr. Mathes, dated January 25, 1967, to his Brief on Review, and incorporated the same therein by reference. The said affidavit, marked “Exhibit A”, appears in the Record at page 133.

On January 11, 1966, Country Life filed its written objection to jurisdiction of the bankruptcy court, and alleging as ground therefor that the debtor’s real property was in the exclusive custody of the Superior Court of San Mateo County. In its written objection to jurisdiction [R. p. 34], Country Life made the following misrepresentations at page 1, lines 25 to 29, inclusive:

“On November 5, 1965, said Superior Court appointed a Receiver to take possession of the said property *and the rents therefrom* in aid of your Respondent’s *foreclosure proceeding*. Said Superior Court, through its Receiver has had custody of said property at all times thereafter.” (Emphasis added).

Since, as previously noted, the Superior Court lawsuit was *not* a “foreclosure proceeding”, and since there were no tenants and, therefore, no rents to be collected, and, in fact, the State Court Receiver never took possession of the property, and never collected any “rents,” the above-quoted language is, at least, highly misleading, if not actually false, irrespective of Referee Bergener’s reluctance to recognize that Country Life’s above representation was something less than accurate. Of course, the legal significance of the misrepresentations made is the fact that under the doctrine of *Emil v. Hanley*

(1954), 318 U.S. 515, 63 S. Ct. 687, 87 L. Ed. 954, if a State Court Receiver *actually* had possession and custody of the debtor's realty pursuant to a *legitimate* foreclosure proceeding, the bankruptcy court could not supplant such Receiver with its own, save in a proceeding under Chapters X or XII. (However even had there been a State Court Receiver in possession pursuant to a legitimate foreclosure proceeding, the bankruptcy court has jurisdiction to restrain the foreclosure proceeding by virtue of Sec. 314 of the Bankruptcy Act).

Although it may be anticipating argument, we feel constrained at this point to submit, in passing, that it is appellant's very definite position that even in ordinary bankruptcy proceedings, a bankruptcy court cannot be deprived of jurisdiction over a bankrupt's real property by the utterly spurious "receivership" present herein, involving the absurdity of a receiver appointed to collect non-existing rents. The bankruptcy court has not merely the power, but the *duty* to pierce such a thin disguised veil of alleged "adverse possession", which is scarcely even "colorable" (2 Collier on Bankruptcy, Para. 23.07 (2), pp. 524, *et seq.*).

With respect to the hearing before Referee Bergener on January 13, 1966, appellant, who was then receiver, was *not* made a party thereto, had *no notice* thereof, *nor opportunity to be heard*, and is, accordingly, *not* bound thereby, under the most elementary principles of due process of law. We will consider this matter in more detail hereinbelow.

In any case, at said hearing, Mr. Mathes announced that he was filing a Petition for Reorganization of the debtor under Chapter X, which, he stated, rendered the

hearing "moot", following which Referee Bergener on the same day, *i.e.*, January 13, 1966, entered an Order [R. pp. 62, 63], as follows:

"ORDERED, that that certain Order issued by this Court under date of January 4, 1966, restraining the San Mateo Title Co. and Country Life Insurance Co., an Illinois corporation, from taking steps to sell or otherwise to enforce the deed of trust referred to in said Order is hereby declared to be dissolved and of no further force and effect."

There was no evidence whatever submitted at the January 13, 1966, hearing, much less evidence establishing lack of equity in the realty, and, as will be demonstrated hereinbelow, there is a vast substantive difference between (1) an order merely dissolving a previous, temporary restraining order, and (2) an order granting affirmative leave to foreclose, the fundamental difference being that the latter type order *requires proof by a preponderance of competent evidence, that no equity exists in the property for the bankrupt or debtor's estate, or the creditors thereof*. It is obviously not the function of a court of bankruptcy to improvidently "give away", or permit to be taken, a substantial equity in a bankrupt or debtor's real property, at least, not without affording every reasonable opportunity, and a reasonable period of time, to attempt to realize such equity as may exist, either by sale or refinancing.

On January 14, 1966, the day after entry of the order of Referee Bergener, set forth hereinabove, Country Life caused First American Title Insurance and Trust Company, hereinafter designated as "First American", as trustee under Country Life's trust deed, to offer

the property for sale, presumably under the power of sale provision of said trust deed. As alleged in Para. XIX of appellant's Application, at said purported sale, First American announced, prior to offering the property for sale, that the owner of the property was in bankruptcy, and that there was some doubt as to whether the sale was proper, and that the property was, therefore, being sold *subject* to the rights of any Bankruptcy Court or Trustee in Bankruptcy. These announcements dissuaded all prospective bidders save Country Life, which proceeded to "buy" the property for \$871,191.97, a figure somewhat below the balance then owing on its first trust deed. First American's deed to Country Life, a copy of which is appended to appellant's Application of June 29, 1966, as "Exhibit A", states on its face the following significant qualification:

"... said sale being made *subject* to the rights of any Bankruptcy Court or Trustee in Bankruptcy." (Emphasis added).

It is submitted that the deed to Country Life did not purport to, and did *not*, transfer or convey the bankrupt estate's interest in the property in issue, and that, at most, said deed merely eliminated all inferior liens and encumbrances existing as of January 14, 1966.

Following the hearing of January 13, 1966, a Chapter X Petition was filed by the debtor and a new restraining order was procured restraining First American from delivering its deed to Country Life. Following dismissal of the Chapter X Petition, and on March 3, 1966 [R. pp. 150-153, incl.], there came on for hearing before Referee Ray H. Kinnison, acting in the temporary absence of Referee Bergener, the matter of

the order temporarily restraining delivery of the deed to Country Life. Again, the trustee in bankruptcy had no notice or opportunity to be heard, and was not a party to the proceeding, and, accordingly, is *not* bound thereby. Also, again, *not* one scintilla of evidence was introduced, much less evidence that there was no equity for the bankrupt estate in the property in issue. As a culmination of the "hearing" which consisted principally of a colloquy between counsel for the then debtor, and counsel for Country Life, Referee Kinnison entered a lengthy Order prepared by counsel for Country Life, which, in substance, amounts to an order granting leave to foreclose *ex post facto*, and, likewise, purporting to validate the Order of Referee Bergener, similarly after the fact. This "Order" is supported by neither findings of fact nor any evidence whatsoever.

It is appellant's position herein (1) that the Order of March 3, 1966, is utterly void and totally improper, and (2) that since it purports to grant Country Life affirmative relief, however improperly, Country Life, by seeking and obtaining same, thereby subjected itself to the court's jurisdiction, absent all other grounds therefor, and cannot now be heard to object to this court's jurisdiction.

As alleged in Para. XXII, and Para. XXIII of appellant's Application of June 29, 1966, following entry of the Order of March 3, 1966, Country Life purported to sell the property in dispute to appellee Sequoia Hospital District, hereinafter referred to as "Sequoia", with an option in favor of Sequoia to purchase the property, said lease-option agreement being dated March 31, 1966, and recorded on April 1, 1966, in the Official

Records of San Mateo County. Sequoia owns a large hospital facility immediately adjacent to the bankrupt's convalescent hospital.

As alleged in Para. XXIII of appellant's Application, Sequoia is *not* a bona-fide purchaser of the real property for value within the meaning of Sec. 21(g) of the Bankruptcy Act (11 U.S.C. Sec. 44(g)) because (1) Sequoia did not pay a "present fair equivalent value" and, at best, would only have a lien on the property to the extent of the consideration actually given before it acquired notice of the bankruptcy proceeding, and (2) Sequoia, in fact, had knowledge of the bankruptcy proceeding prior to March 31, 1966.

Incomprehensibly, Title Insurance and Trust Company apparently issued a policy of title insurance to Sequoia.

Extra-Judicial Sales of Real Property After Bankruptcy Without Permission of the Bankruptcy Court, Though Not Void, Are Voidable Where (1) There Is Any Equity in the Property, and/or (2) Where Any Fraud or Other Inequity Is Present.

Thus, in 5A Remington on Bankruptcy, Sec. 2357, page 80, the rule is stated as follows:

"Foreclosure proceedings may not be instituted while the property is in the custody of the bankruptcy court without leave of such court, even though the property lies in another district."

In the same volume of Remington on Bankruptcy, Sec. 2374, the following appears at pages 119, 120:

"Unless the court consents, subsequent attempted foreclosures are void or subject to avoidance *even though not stayed or enjoined.*" (Emphasis added).

As authority for the foregoing statement, the editors cite, in Footnote No. 8, page 120, *Re Hasie* (D.C., Tex., 1913), 206 Fed. 789, in which a post-bankruptcy sale by the trustee under a deed of trust was held *void*.

A similar view is expressed in 8 Collier on Bankruptcy, Para. 3.22, p. 264, Footnote No. 10, under the heading: "Effect of failure to stay":

"... and it cannot be argued that where no stay has been entered a lien may be enforced upon property in the debtor's possession without leave of the court. *Lockhart v. Garden City Bank & Trust Co.*, (C.C.A. 2d., 1940) 4 Am. B.R. (N.S.) 594, 116 F. 2d 658. Contra: *Matter of Potts*, (E.D. Ky., 1942) 51 Am. B.R. (N.S.) 368, 47 F. Supp. 990."

The cases urged by Country Life, as assertedly supporting a contrary rule, are, in fact, *not contra* to the general rule as quoted hereinabove from both Collier and Remington, but represent a variant or "exception" to the rule based solely upon the peculiar, and similar facts involved in those cases, facts which, literally, are diametrically different from the facts involved herein.

Thus, in *Hardt v. Kirkpatrick* (9th Cir., 1937), 91 F. 2d 875, the basis of the decision appears on pages 879, 880:

"In his answer to the Appellee's petition for an injunction, the Appellant averred under oath that the amount bid and paid for the real property and water stock, \$5,250.00, 'was and ever since has been far in excess of the value of said real property and water stock, and said sale was in all respects fair and regular'. In his brief, the Appellee con-

cedes that 'in this case the market value was paid for the property', but argues that 'paying a reasonable price cannot validate illegal taking of property from the jurisdiction of the court'.

"In the language of *Hiscock v. Varick Bank*, supra (206 U.S. 28), in the instant case there is no 'fraud or a proceeding contrary to the contract' as a result of which 'the interposition of the court might properly be invoked'. Therefore, 'in the absence of factors requiring interference, a court of bankruptcy will not disturb the foreclosure of a lien by non-judicial action when such foreclosure is in accord with the agreement of the lienor and lienee'." (Emphasis added).

In *Heffron v. Western Loan & Building Co.* (9th Cir., 1936), 84 F. 2d 301, the court said at page 304:

"It is, of course, an incident of the bankruptcy court's jurisdiction that such private sales are (sic, 'as'?) those in the *Hiscock* and *Robinson* cases, and in the case before us *may in such circumstances be enjoined before made or set aside after completion in the discretion of the bankruptcy court*. The sale may have been fraudulent or possess the characteristics of a preference. Again, the court may force the creditor-lienee to pursue his lien in the bankruptcy proceedings rather than *aliunde*, inasmuch as a greater equity in the property may be preserved in this manner for the general estate. *But these are matters for the discretion of the court.* (Citations omitted). *The trustee in this case has urged no particular factors militating against the particular trustee's sale sought to be*

voided, but bases his argument entirely upon the contention that, once a petition in bankruptcy has been filed, a sale dehors the bankruptcy proceeding is utterly void." (Emphasis added).

Obviously, all that the court held in the *Hardt* and *Heffron* cases, *supra*, was that where, unlike the instant case, *there is clearly no substantial equity for the bankrupt estate in and to the real property in question, and no fraud, inequity or other conduct requiring judicial interference*, courts are not going to exercise the idle and pointless act of setting aside a post-bankruptcy sale, even though technically voidable, where no substantial benefit could accrue therefrom to the bankrupt estate or its creditors. To have done so, in such circumstances, would have been an "exercise in futility". Furthermore, the court expressly pointed out that there was no fraud or misrepresentation involved, as in the instant case, and the overwhelming implication is that the court would not have hesitated to avoid the sales had there been either (1) a substantial equity in the property for creditors, or (2) fraud or inequity present, or (3) both, as is true in the instant matter.

Again, it is clear that the decisions in the *Hardt* and *Heffron* cases, *supra*, clearly represent "exceptions" to the general rule, and must be held to their peculiar facts, *i.e.*, situations in which there is no equity, fraud or other reason warranting avoidance of otherwise regular post-bankruptcy sales.

A decision involving facts more analogous to those of this case, though *not* involving fraud, is *In re Holstein Harvey, Inc.* (D.C., Del., 1928), 28 F. 2d 798, in which a state court foreclosure action was commenced

on the same day on which the bankruptcy petition was filed. The court held that since there was a substantial equity involved, the foreclosure proceedings should be enjoined. In this connection the court held, as follows, at page 799:

“It appears from the oral evidence submitted in open court by the petitioner that the bankrupt estate has a very substantial equity in the property. . . . In view of these facts it appears that the court of bankruptcy has without doubt jurisdiction to enjoin the sale under foreclosure proceedings instituted in the state court on the very day that the petition in bankruptcy was filed. *First Trust Co. v. Baylor*, 1 F. 2d 24 (C.C.A. 8); *Britton v. Western Iowa Co.*, 9 F. 2d 488, 45 A.L.R. 711 (C.C.A. 8); *First Sav. Bank & Trust Co. v. Butler*, 282 F. 866 (C.C.A. 8).”

To summarize the foregoing, while an extra-judicial postbankruptcy sale, conducted without the permission of the bankruptcy court, is *voidable*, and *will* be set aside on any showing of a substantial equity in the property, fraud, inequity, etc., nevertheless, absent any such factors, a court will not void a sale where no real benefit would result therefrom to the bankrupt estate, merely to satisfy the whim of the trustee in bankruptcy, or to enable him to thereby attempt to extort a “settlement” offer from the hapless secured creditor (See, further, 3 Collier on Bankruptcy, para. 57.20, at p. 314).

A further cogent distinction between this case and the *Hardt* and *Heffron* cases, *supra*, lies in the fact that those proceedings were ordinary bankruptcy proceed-

ings, whereas, at the time the order of January 13, 1966 was procured herein, this was a proceeding under Chapter XI of the Bankruptcy Act. As will be demonstrated hereinbelow, by virtue of Section 311, the basis of summary jurisdiction in a Chapter XI proceeding is *either* title or possession. Thus, where, as here, a debtor incontestably had title to the real property in issue at the date of the petition, the court *ipso facto* acquired summary jurisdiction of *all* its property "wherever located", and it would seem to follow therefrom that any attempted foreclosure or other sale thereof, without the court's permission, would be *void*, not merely voidable, as in an ordinary bankruptcy proceeding where the court's permission is not obtained.

See, also, 8 Collier on Bankruptcy, Para. 3.22(2), p. 272, in which the editors, after a thorough discussion of the issue, conclude as follows:

"And a reasonable synthesis of these cases, in light of the principles involved, would be that the secured creditor, as to collateral in the custody of either the court or the debtor in an arrangement proceeding, *must first procure the permission of the court to foreclose thereon.*" (Emphasis added).

The Order of January 13, 1966, Did Not Grant Leave to Foreclose; Furthermore, Said Order Was Procured, at Least in Part, by Misrepresentations.

As previously noted, Referee Bergener's Order of January 13, 1966, merely dissolved the temporary restraining order procured by the debtor on January 4, 1966, and nothing contained in said Order could even remotely be construed to constitute an affirmative order granting Country Life leave to foreclose, or to sell the debtor's property under the power of sale.

Since Country Life caused (“forced” might be a more accurate word) the trustee under its deed of trust to sell the property in issue, the very day after entry of Referee Bergener’s Order of January 13, 1966, despite serious, and we submit, legitimate misgivings on the part of said trustee, no rational inference can be logically drawn therefrom, *save and except that at all times, Country Life intended to cause the property to be so sold* as soon as it could procure any order from the bankruptcy court which might appear, even colorably, to legitimize such sale.

There is, we submit, a vast and very real substantive distinction between (1) an order refusing to continue an injunction (based upon the assumption that the property) was in the jurisdiction of the state court), and (2) an order granting a secured creditor leave to foreclose on its security, whether by judicial foreclosure or by trustee’s sale under the power of sale, on the basis of an apparent lack of equity. What Country Life, in fact, did was to procure the first type of order (based on misrepresentations), when it intended to conduct a non-judicial sale under the power of sale contained in its trust deed, a type of order (No. 2, *supra*) which could *only* be procured legitimately upon proof satisfactory to the bankruptcy court, that no equity existed in the property for the bankrupt’s general creditors.

To summarize the foregoing, what Country Life did was to procure an Order vacating an injunction, based in part upon misrepresentations that the property was in the exclusive jurisdiction of a state court in connection with foreclosure proceedings, when, in truth and in fact, Country Life *intended* to have the property sold

extra-judicially (which conclusively gives the lie to any claim that the property was in the state court's jurisdiction), which said extra-judicial sale would *only* be proper on proof of want of equity, as a consequence of proceedings for leave to foreclose, and, of course, following due and proper service on the then receiver, who most obviously was, and is, a necessary party to any such proceeding.

By urging that the debtor's real property was in the custody of a state court receiver when, in fact, said receiver had never taken possession of the property nor collected any rents, since there were no tenants and hence no rents to be collected, and by failing to advise the court that it actually intended to cause the property to be sold extra-judicially, rather than in a "foreclosure proceeding", Country Life not only seriously misrepresented the true facts (despite the Referee's attempt to gloss over this issue at p. 5 of his Certificate on Review [R. p. 67, lines 3-7, incl.], but County Life was merely "playing one court against another", and acting in dubious faith as to both. Since it caused the property to be sold extra-judicially on the day after the January 13, 1966 hearing, it can scarcely be conceived that Country Life did not so intend to proceed at the time of the hearing, and hence its failure to so advise the court coupled with its false, written representation that its Superior Court action was a "foreclosure proceeding", if not a fraud, certainly casts a taint on the order so procured regardless of the Referee's apparent aversion to recognize that Country Life's conduct falls short of the standards normally enforced in courts of equity.

Fraud or misrepresentation will vitiate even what might otherwise be a valid, if technical, objection to the summary jurisdiction of the bankruptcy court. Thus, in *In re Southern Metal Products Corp.* (D.C., Ala., 1939), 26 F. Supp. 666, the court held: (1) In summary proceeding by bankruptcy trustee to compel a receiver appointed by the state court, in proceedings to foreclose a mortgage executed by the bankrupt, to turn mortgaged property over to the trustee, the bankruptcy court could inquire into the receiver's claim to the property for purposes of ascertaining whether the summary proceeding was appropriate and could determine whether the trustee's claim was real or merely colorable; (2) the bankruptcy referee has jurisdiction to summarily order a state court receiver to surrender to a bankruptcy trustee, property which had been placed in the possession of such state court receiver in a proceeding to foreclose a mortgage, where execution of the mortgage and institution of the foreclosure and appointment of a receiver were an attempt by the mortgagee to secure an advantage over the bankrupt's other creditors with intent to hinder, delay or defraud the latter.

Certainly the rationale of the decision in *Southern Metal Products* has application here in light of the fact that the order appointing the state court receiver to collect non-existing rents can have no rational explanation save as an attempt to deprive the bankrupt and its creditors, not to mention the junior encumbrancers, of the only avenue whereby the equity in the property could be salvaged.

In Chapter XI, Unlike Ordinary Bankruptcy Proceedings, the Debtor's Ownership of Property Is Sufficient to Confer Upon the Bankruptcy Court Summary Jurisdiction to Adjudicate Controversies Arising Therefrom.

The law is stated in 8 Collier on Bankruptcy, Para. 3.02, pp. 176, *et seq.*, as follows:

"Section 311, gives the court in which the petition is filed 'exclusive jurisdiction of the debtor and his property, wherever located'. *That jurisdiction over property rests on ownership of property, as distinguished from possession.* There is no comparable provision in Chapters I to VII. With some exceptions, where a third party to an ordinary bankruptcy proceeding under Chapters I to VII has possession of the property and asserts a substantial adverse claim thereto, the bankruptcy court does not acquire summary jurisdiction over a controversy with respect to the property, even though ownership of the property is in the bankrupt. *As a result of Sec. 311, however, the court in a proceeding under Chapter XI has summary jurisdiction in that situation.*" (Emphasis added) .

The editors proceed to point out at pages 179 through 180, that a Chapter XI court also has summary jurisdiction over property in possession of the debtor, as in ordinary bankruptcy proceedings, irrespective of ownership, and points out, at p. 181:

"Under Sec. 311, *either* ownership in the debtor at petition filed, or possession of the court, is a basis for summary jurisdiction over controversies." [Emphasis added).

Concluding the discussion of this issue, the editors state the following at page 182, with reference to the “extension” of summary jurisdiction under Sec. 311:

“The only extension in summary jurisdiction made by Sec. 311, is to give the bankruptcy court summary jurisdiction over controversies with respect to property in the possession of a third party who does not assert a substantial claim of ownership thereto, although such third party does assert other substantial claims against that property.”

Applying the foregoing rules to the instant case, it is submitted that it is undisputed that ownership to the real property in controversy was in the debtor as of the date of bankruptcy. Accordingly, the bankruptcy court had, and still has, summary jurisdiction to determine any and all controversies with reference thereto. It is further submitted (1) that the state court did *not* have possession, (2) that Country Life had no intention to foreclose judicially, indeed, could *not* have done so since its action was for “Specific Performance”, as distinguished from a foreclosure proceeding, and (3) that the alleged rule that once having given up possession, the court cannot reacquire the same has *no* application where the order pursuant to which the extra-judicial sale was held, was procured by a fraud on the court, or any inequitable conduct proximating fraud. (See *Parker v. Checker Taxi Co.*, 238 F. 2d 241).

Although as previously noted, the jurisdiction of a court of bankruptcy is even more pervasive in a Chapter XI proceeding than in an ordinary bankruptcy proceeding, because title to real property in the debtor, regardless of “possession”, is, itself, sufficient to confer

upon the court summary jurisdiction, nevertheless, this court had, and has, jurisdiction over the realty involved in the instant case in any case, because the so-called state court "receivership" was so obviously spurious, if not fraudulent, that the alleged "adverse" claim cannot be regarded as more than "colorable", if that. Furthermore, since the property was vacant at the date this proceeding was commenced, it was, accordingly, in the constructive possession of the debtor and this court. (See, generally, 5 A Remington on Bankruptcy, Sec. 2361, p. 94; also, Sec. 2374, pp. 118, 119).

Additionally, even assuming, *arguendo*, that the state court receiver *had* taken possession of the debtor's realty (which was *not* the fact), even in such circumstances, it is doubtful that such assumed fact would deprive this court of jurisdiction, since the action was *not* a "foreclosure proceeding", and appellees, thus far at least, have been unable to cite a single decision holding that a non-foreclosure, state court receivership deprives the bankruptcy court of jurisdiction.

However, recognizing the more pervasive jurisdiction under Chapter XI than in so-called "straight bankruptcy", appellees belatedly (after two (2) sessions of oral argument and one set of Points and Authorities), have asserted the wholly groundless argument that the proceeding was "converted" to an ordinary bankruptcy proceeding on January 13, 1966, because the debtor's counsel inadvertently filed with the debtor's schedules the printed first page Wolcott form, which, of course, is appropriate for an ordinary, voluntary proceeding, but inappropriate to an arrangement proceeding. Not only did counsel for the debtor and the court recognize and treat the case as a Chapter XI proceeding at all

times, but so also did counsel for Country Life. Thus, in the latter's Reply Memorandum filed as late as February 15, 1966 [R. pp. 147, 148], the following significant language, which is totally inconsistent with its recent argument, appears at page 1, lines 28 to 31, inclusive, as follows:

"Accordingly, the Court should disapprove the Chapter X petition and dismiss the same, *leaving this case in the posture it was under (sic) Chapter XI proceeding at the time the Chapter X was filed.*" (Emphasis added).

The Fact That the Receiver Was Not a Party to the Proceedings Resulting in the Orders of January 13, 1966, and March 3, 1966, Renders Such Orders Void and Wholly Ineffective as Against Him.

In 9 Collier on Bankruptcy, Para. 10.10, the following is set forth at page 510:

"Any authorized act by a *debtor in possession* is binding, *in the absence of unusual circumstances*, upon the trustee in the subsequent bankruptcy administration of the proceeding." (Emphasis added).

Obviously, in this case, there was no "debtor in possession" as the present trustee was appointed receiver on January 6, 1966, two (2) days after the petition was filed, and seven (7) days prior to the hearing of January 13, 1966. Also, obviously, it is an utter understatement to say that there was *very* "unusual circumstances" involved in this case.

Since a "debtor in possession" is expressly accorded "all the powers of a trustee appointed under this Act" (Sec. 342), obviously, a final order entered in a pro-

ceeding or hearing to which he is a party, will, in the absence of "unusual circumstances", be binding on a trustee in bankruptcy appointed after the debtor is adjudicated a bankrupt. However, it is equally obvious *that such rule is limited by definition to a "debtor in possession"*, and where, as here, a receiver is appointed, the latter is most certainly *not* bound by an order entered as a consequence of litigation between the debtor and some third party or parties, to which the receiver was not made a party. To hold otherwise would run afoul of the most elementary principles of due process of law. Furthermore, Country Life's complaint that it did not initiate the proceeding out of which the order of January 13, 1966 arose, is no answer at all. Not only should Country Life have brought on proper proceedings for leave to foreclose, but it should also have joined the receiver. Of course, Country Life could not have successfully maintained such a proceeding in light of the very substantial equity in the real property in issue, which fact, presumably, led to its attempt to achieve the same general result by making the misrepresentations heretofore enumerated.

As previously pointed out, there is a vast distinction between an order denying an injunction, based upon representations that real property is in the jurisdiction of a state court receiver in connection with *foreclosure proceedings* commenced prior to bankruptcy, and a petition for leave to foreclose. The latter requires *proof* of lack of equity, which could *not* have been adduced in this case, whereas, of course, the former type of order does not. Again, these considerations amply point up the grave inequity and injustice to the debtor's estate, its creditors, and the junior encumbrancers,

which, unless corrected, has deprived them of the very substantial equity which exists in the real property involved herein.

Since a Chapter XI receiver has the same powers, duties and rights as a trustee in bankruptcy by virtue of Sec. 341 and Sec. 352 of the Bankruptcy Act, the conclusion appears inescapable that such a receiver *must* be made a party to any proceeding out of which an order is entered which divests, or purports to divest, the debtor's estate of property, be it real or personal. To hold otherwise would deprive the receiver, and more particularly, the creditors for whom he is legal representative, of property without due process of law. It is clear, if citation of authority were even necessary, that the constitutional guarantee of the due process clause of the Fifth Amendment to the United States Constitution applies to bankruptcy proceedings (*Louisville Joint Stock Land Bank v. Radford* (1935), 295 U.S. 555, 55 S. Ct. 854, 79 L. Ed. 1593; *Alexander v. McDonald* (5th Cir., 1941), 120 F. 2d 72, 73; *In re Rosser* (8th Cir., 1900), 101 Fed. 562, 568; *In re Stephens* (D.C., Tex., 1961), 211 F. Supp. 201, 202; *Hess v. Amidon* (1937), 56 Ohio App. 99, 10 N.E. 2d 26, 28, cert. den., 302 U.S. 706, 58 S. Ct. 26, 82 L. Ed. 546).

In *Alexander v. McDonald*, *supra*, the court held as follows, at page 73:

“The record is brief and contains only the pleadings and Orders in the case and several exhibits. We have carefully examined the record and failed to find that Alexander was ever given a hearing or ever notified of any hearing or proceeding affecting his alleged title to the land. All that appears is the unsupported report of the Referee in

which he states that at some previous time, while acting as Conciliation Commissioner, he heard sworn testimony which convinced him that title to the land was in McDonald. This will not do. *Title to property claimed to be owned by a bankrupt may not be adjudicated in such a way. Alexander was and is entitled to have notice of any hearing affecting title to the land so that he might have an opportunity to present whatever evidence of title he might have, with the proceedings subject to review by the District Court. Any other method would be sheer denial of due process of law.*" (Emphasis added).

In light of the foregoing, the language of Referee Bergener's Order of October 28, 1966, to the effect that the Orders of January 13, 1966, and March 3, 1966, had become "final", is obviously violative of the due process clause *to the extent that it purports to hold said Orders "final" and binding as against appellant as receiver, and subsequently trustee in bankruptcy, since he was not a party to the proceedings out of which said Orders issued, and had neither notice nor opportunity to be heard.* Furthermore, the reference to the "finality" of the aforesaid Orders in the Order of October 28, 1966, totally conflicts with the final paragraph thereof, which purports not to "prejudice" the right of appellant to institute "any action or proceeding in a court of appropriate jurisdiction", etc. This latter provision is illusory, since if the Order were allowed by appellant to stand unchallenged, it might well be held *res judicata* so as to bar any right to raise the serious constitutional issues of due process with respect to the Orders of January 13, 1966, and March 3,

1966. In short, the Order of October 28, 1966, is a contradiction on its face, and this fact alone constitutes one of the several glaring flaws in the "theory", suggested in the Certificate on Review, that the Referee had "discretion" to decline to exercise jurisdiction, which "theory" will be considered more fully hereinbelow. These observations, of course, apply with equal force to the District Court's Order of March 8, 1967 [R. pp. 484, 485], insofar as it holds that appellant is bound by the aforementioned Orders.

By Its Action in Seeking Affirmative Relief Herein, Country Life Thereby Consented to the Jurisdiction of the Bankruptcy Court.

Entirely aside from all the reasons heretofore reviewed, which establish the jurisdiction of the bankruptcy court over the real property in issue, a further basis therefor clearly exists as a consequence of the fact that Country Life sought, and was granted, affirmative relief in connection with the Order of March 3, 1966.

The law respecting submission to jurisdiction by consent is well stated in 2 Collier on Bankruptcy, Para. 23.08(5), at pages 547, *et seq.*, as follows:

"When an adverse claimant to property voluntarily submits the question of his claim for determination by the bankruptcy court, jurisdiction is conferred by consent and the trustee or receiver cannot be heard to object. Nor may the claimant himself thereafter question the exercise of such jurisdiction. (Citing Footnote No. 59, page 548, *inter alia*: *Barringer v. Lilley*, (9th Cir., 96 F. 2d 607)) Thus a mortgagee who petitions the bank-

ruptcy court for payment of the mortgaged debt thereby consents to the court's summary jurisdiction to determine the validity of the mortgage. (Citing, Footnote No. 60, page 59: In re Platteville Foundry & Machine Co., (D.C., Wis.) 147 Fed. 828, and cases there cited; In re Durham, (D.C., Md.) 114 Fed. 750; Chauncey v. Dyke Bros., (8th Cir., 119 Fed. 1). Also, likewise a defendant who seeks affirmative relief by a cross motion or other appropriate pleading thereby consents to the jurisdiction of the court. (In re Engineers Oil Properties Corp., (D.C., N.Y., 1947) 72 Fed. Supp. 989." (Emphasis added).

See, also, *Matter of Morris White Holding Co., Inc.* (D.C., N.Y.), 52 F. 2d 499, in which the court held that a mortgagee's filing of a petition to allow foreclosure in another proceeding constituted a submission to the jurisdiction of the bankruptcy court, and made it a party to the bankruptcy proceedings.

Applying the foregoing rules to the facts of this case, it is submitted that in substance Country Life procured an order (of March 3, 1966) granting it leave to foreclose, albeit *ex post facto*, and without a scintilla of evidence of any character whatsoever, much less evidence that no equity existed in the property for the then bankrupt estate. Again, appellant was *not* a party thereto.

It is further submitted that, if anything, the order of March 3, 1966, is even more improper than that of January 13, 1966, since, as above-noted, it amounts, in substance and effect, to an order *retroactively granting leave to foreclose by an extra-judicial sale, without any evidence whatever to support it.*

The following language from the order, obviously prepared by counsel for Country Life, clearly supports the foregoing analysis. Thus, at page 3 [R. p. 152], lines 20 to 26, inclusive, appears the following:

“ . . . but that Country Life Insurance Co., an Illinois corporation, and First American Title Company, as trustee under the said deed of trust, *should be permitted to enforce the above referred to deed of trust in accordance with the terms thereof and the laws of the State of California, free of any restraint by the bankruptcy court.*” (Emphasis added).

In the order itself (the above quotation being from the lengthy preamble) it provides as follows [R. pp. 152-153]:

“ORDERED, that all restraining orders heretofore issued in the above proceeding *are declared to have expired of their own force, and that at the present time there are no restraining orders in effect in the above entitled proceeding*; without limiting the generality of the foregoing, the order of January 17, 1966, restraining First American Title Insurance & Trust Company and/or San Mateo County Title Company, as trustee, from delivering the deed evidencing the sale of the real property under the power of sale contained in the above referred to deed of trust, *is declared to be of no present effect*; and it is further

“ORDERED, that Country Life Insurance Co., an Illinois Corporation, First American Title Insurance & Trust Company and/or San Mateo County Title Company, as trustee, *may proceed forthwith to enforce the deed of trust hereinabove*

referred to in accordance with the laws of the State of California, free of any further restraint by the Bankruptcy Court, without limiting the generality of the foregoing, First American Title Insurance & Trust Company and/or San Mateo County Title Company, as trustee, may deliver its trustee's deed evidencing the sale conducted under the power of sale contained in the deed of trust above referred to." (Emphasis added).

Certainly, by any reasonable construction, the above-italicized language constitutes the granting of affirmative relief to Country Life, even though wholly improperly, since it had adduced no evidence whatever that there was no equity for the bankrupt estate in the real property affected. This egregious impropriety in the order does *not*, however, alter the fact *that affirmative relief was very definitely sought by, and granted to, Country Life*. Accordingly, absent all the other grounds therefor, it is submitted that by seeking the affirmative relief of the Court, Country Life thereby clearly submitted itself to the court's jurisdiction, and *cannot* be heard now to object thereto.

The Trustee's Deed to Country Life Was Expressly Subject to the Interest of the Bankrupt Estate.

As alleged in appellant's Application of June 29, 1966, [R. p. 235, *et. seq.*] and as evidence by the trustee's deed appended thereto as "Exhibit A" [R. pp. 249, 250], on its very face, the deed from the First American Title Insurance and Trust Company to Country Life, expressly provides, as follows:

"... said sale being made *subject* to the rights of any Bankruptcy Court or Trustee in Bankruptcy." (Emphasis added).

It is submitted that Country Life, at most, merely eliminated the junior liens, and did *not* acquire the title that clearly stood in the bankrupt (then debtor) at the commencement of this proceeding on January 4, 1966, since the above deed was made explicitly *subject* to the title of this bankrupt estate. Furthermore, by virtue of the above-quoted language of the trustee's deed, Sequoia had at least constructive, if not actual, notice of the interest of this bankrupt estate in and to the real property here in issue.

The Facts of This Case Require the Court's Exercise of Its Exclusive Jurisdiction, and Preclude Any "Discretion" to Decline to Exercise Same.

As heretofore noted, the Referee suggests in his Certificate on Review, that an alternative basis for his Order of October 28, 1966, was an exercise of "discretion" to decline to exercise what we submit was an exclusive jurisdiction over the real property in dispute, so as to permit the matter to be determined, presumably, in the Superior Court of San Mateo County (hardly a convenient forum for the trustee of a presently "no-asset" bankrupt estate pending in the federal court in Los Angeles).

As, also noted previously, the provision that the order in question is "without prejudice" to appellant's right to relitigate the matter elsewhere is highly chimerical and a contradiction in terms, in view of the implicit finding that the Orders of January 13, 1966, and March 3, 1966, are "final", as against appellant, notwithstanding that he was not a party to the proceedings out of which said Orders arose, and had neither notice nor opportunity to be heard in connection therewith, since such finding, if not directly attacked, would probably become *res judi-*

cata, precluding appellant from raising this vital issue of constitutional law in any other forum.

In addition to the foregoing defect in the “theory” that the Referee could properly decline to exercise jurisdiction in his “discretion”, it is submitted that the facts of this case are such as to fall within the general rule that exclusive jurisdiction may *not* be surrendered, rather than the narrow “exception” thereto which recognizes such “discretion” where (1) *the best interests of the estate* and all of the parties would be served by allowing the matter to be litigated in a state court; and (2) where the central issue is *some doubtful question of State law*. Neither criteria is applicable in the instant case.

As noted in 1 Collier on Bankruptcy, para. 2.07, pages 156, 157; 5A Remington on Bankruptcy, Sec. 2384, page 135; and 8 Collier on Bankruptcy, para. 301, page 170, generally the exclusive jurisdiction of the bankruptcy court may *not* be surrendered. (*Gross v. Irving Trust Co.* (1933), 289 U.S. 342, 53 S. Ct. 605, 77 L. Ed. 1243; *Isaacs v. Hobbs Tie & Lumber Co.* (1931), 282 U.S. 734, 51 S. Ct. 270, 75 L. Ed. 645; *U.S. Fidelity & Guaranty Co. v. Beay* (1912), 225 U.S. 205, 32 S. Ct. 620, 56 L. Ed. 1055). An “exception” to said general rule is recognized where (1) *the best interests of the estate* and all of the parties concerned would be served by allowing the matter to be litigated in a state court, and (2) where some doubtful or unresolved question of state law is involved. This was the rationale of *Thompson v. Magnolia Petroleum Co.* (1940), 309 U.S. 478, 484, 60 S. Ct. 628, 84 L. Ed. 876, cited in the Referee’s Certificate, and all similar cases.

In all cases in which the trustee was required or directed to proceed in the state courts, there was involved some point of state law which was unsettled, and which the federal courts felt should properly be determined by the state courts in the first instance. Thus, in *Thompson, supra*, there was a question as to title under state law to rights of way land; in *Mangus v. Miller* (1942), 317 U.S. 178, 185, 63 S. Ct. 182, 87 L. Ed. 169, there was uncertainty as to state law concerning the effect of a default under a land sale contract involving joint tenant vendees; in *Gramil Weaving Corp. v. Reindeer Fabrics, Inc.* (2nd Cir., 1950), 185 F. 2d 537, 540, the title to certain goods, sold by the bankrupt and under attachment, was uncertain under state law; in *Matter of East Coast Ry. Co.* (D.C. Fla., 1943), 149 F. Supp. 527, the trustee's liability for state taxes was uncertain because the state courts had not construed the tax statutes involved, etc.

That the remission of matters for determinations by state courts represents the "exception", and *not* the rule, was emphasized by Mr. Justice Black, in the *Thompson* opinion, *supra*, for he expressly reaffirmed the principle that the bankruptcy or reorganization court has "an exclusive and non-delegable control over the administration of an estate in its possession." The editors of Collier similarly emphasize the normal applicability of the general rule. Thus, in 1 Collier on Bankruptcy, para. 2.07, the following appears at pages 161, 162:

"On the other hand, where it is clear that state court decisions have removed an determinative uncertainty as to the state rule applicable, say, in a property question, the parties should *not* be

remitted to a state court for a disposition of the controversy. (Citing, *inter alia*: *Matter of Chicago & Northwestern Ry. Co.*, (7th Cir., 1942) 127 F. 2d 1001, cert. den., 317 U.S. 659, 63 S. Ct. 59, 87 L. Ed. 529)". (Emphasis added).

See *Stout v. Green* (9th Cir., 1942), 131 F. 2d 995, holding that a dispute arising from the non-payment of a state liquor license fee by the trustee, and the assertion of a lien for unpaid alcohol taxes need not be remitted to the state court.

The following authorities and decisions clearly support the view that the "discretion" to require the trustee to proceed in a state court is narrowly limited to situations in which (1) *the best interests of the estate* would be served, and (2) where the central issue is an unresolved question of state law:

(1) *In Matter of Chicago & Northwestern Ry. Co.*, *supra*, 127 F. 2d 1001, the court stated the following at p. 1004:

"Neither applicable statutes nor decisions of Illinois were available at the time *Thompson v. Magnolia Petroleum Co.* was before the Supreme Court. And the difficulties of determining just what should be the decision under Illinois law were persuasively indicated by the different results reached by the two Circuit Courts of Appeal that had attempted determination. The Supreme Court refused to resolve this conflict in order that the important question of property law might not—by accident of federal jurisdiction—be resolved in a way that might prove contrary to the result of some subsequent state court. Accordingly, the court held that the bankruptcy court had abused its dis-

cretion by not sending the matter to the appropriate state court. *However, in our case, no more uncertainty attends the disposition than is present in the decision of most legal questions.*

“Clearly in the light of recent Illinois decisions, there is no such uncertainty as to require sending the case to the state court. *If the matter were referred to the state court, the one certain result would be an increase in the costs of litigation, costs which would diminish the estate of the bankrupt. To refer to the state courts every land question arising in bankruptcy would be to disregard the very objectives of the summary jurisdiction granted to the bankruptcy court. Such was not the rule of the Magnolia case.*” (Emphasis added).

(2) *In Matter of J. Rosen & Sons, Inc.* (3rd Cir., 1942), 130 F. 2d 81, a Referee was reversed for “surrendering” jurisdiction over a real property dispute arising in a Chapter XI proceeding, and the Court of Appeals holds as follows, p. 82 and p. 84:

“A court of bankruptcy has summary jurisdiction to determine controversies in regard to property of which it has possession. *The validity of the mortgage should have been decided promptly unless that decision required a determination of an unsettled question of New Jersey law. It was the duty of the Referee promptly to dispose of the questions presented by the petitions of the trustee and Reconstruction Finance.*

“*If the Referee was unable to decide these questions, the learned District Judge should have done so. . . . An order granting authority to the Reconstruction Finance Corporation to foreclose its mort-*

gage in the state court should have been made *only after an express finding by the court that the mortgage was valid.*" (Emphasis added).

See, also, *In re Fine Arts Corporation* (6th Cir., 1943), 136 F. 2d 28, 30, 31.

Applying the foregoing principles to the facts of the instant case, it is submitted (1) that the "best interests" of the bankrupt estate would most definitely *not* be served by requiring appellant to try the case in San Mateo County, involving as it necessarily would, undue delay not to mention costs, which appellant would either have to advance personally, or attempt to solicit from some or all of the creditors; and (2) there is not only no unsettled issue of state law involved, but to remit appellant to the state court would deprive him of his two strongest positions, viz.: (a) the constitutional question of due process, and (b) the issue of "equity" in the realty.

With respect to the latter point, the existence of the substantial equity in the property is immaterial under state law, but of vital moment under Chapter XI, since the bankruptcy court has a duty to afford a debtor a reasonable opportunity to realize an equity in its real or personal property, to which end it may restrain foreclosure proceedings. In contrast, under the law of California, as well as most states, the existence of even a substantial equity is technically irrelevant and, in itself, no defense to a foreclosure proceeding. Thus, if a mortgage or trust deed is, in fact, in default, and if all the technical prerequisites to foreclosure, or sale under the power of sale, have been met, the fact that even a most substantial equity exists in favor of the hapless mortgagor or trustor is immaterial. Thus, to

remand appellant to the “tender mercies” of state law would deprive him of his strongest position, and, obviously, by no process of logic could such be characterized as being in the “best interests” of the bankrupt estate or its creditors.

Conclusion.

For all of the foregoing reasons, it is respectfully submitted that the District Court’s Order of March 8, 1967, as well as the Referees’ several Orders of January 13, 1966, March 3, 1966, and October 28, 1966, should be reversed, and it should be decreed that the real property in controversy is an asset of the bankrupt estate subject only to the existing encumbrances of record.

Respectfully submitted,

JOSEPH S. POTTS,

Attorney for Appellant.

Certificate.

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

JOSEPH S. POTTS

